

**A Report on the Feasibility of Public-Private
Partnerships to Finance Required Facilities and
Related Capital Expenses for the Departments of
Corrections, Juvenile Justice, Military Affairs,
and State Police**

**Submitted by the Secretary of Public Safety to the Governor
and Chairmen of the Senate Finance and House
Appropriations Committees: Pursuant to Item 401.D of the
2003 Appropriation Act**

October 15, 2003

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Introduction

In 2002, the Virginia General Assembly enacted the Public-Private Education and Infrastructure Act (PPEA). This new law allows public entities to accept solicited or unsolicited proposals from private entities to acquire, design, construct, improve, renovate, expand, equip, maintain, or operate qualifying projects.

Code of Virginia, Section 56-575.2 outlines the declaration of public purpose for this new law. The basic elements of its purpose as set forth by the General Assembly are as follows:

- There is a public need for timely delivery of education and other government facilities and other public infrastructure;
- This need may not be wholly satisfied by existing methods of procurement;
- There are inadequate resources to meet these needs and there is demonstrated evidence that public-private partnerships can improve the schedule for delivery, lower the cost, and provide other benefits to the public;
- Tax incentives exist that promote public entities to enter into public-private partnerships; and
- Authorizing private entities to act under the PPEA may result in more timely or less costly availability of projects, thereby serving the public safety, benefit and welfare.

The 2003 Acts of Assembly, Chapter 1042, Item 401.D (see below) directed the Secretary of Public Safety, with the assistance of the Departments of General Services and the Treasury, to examine the feasibility of public-private partnerships as a method of providing required facilities and related capital expenses for the Departments of Corrections, Juvenile Justice, Military Affairs, and State Police, and to report on the findings.

“The Secretary of Public Safety, with the assistance of the Departments of General Services and the Treasury, shall examine the feasibility of public-private partnerships, pursuant to the Public-Private Education Facilities and Infrastructure Act of 2002 (section 56-575.1 et. seq., Code of Virginia) to finance required facilities and related capital expenses for the Departments of Corrections, Juvenile Justice, Military Affairs, and State Police. The Secretary shall include within this examination an analysis of the costs and benefits of public-private partnerships compared to traditional bond financing and cash appropriations on a net present value basis. The Secretary shall provide a report on his findings to the Governor and the Chairmen of the Senate Finance and House Appropriations Committees by October 15, 2003.”

Qualifying Projects

For a project to be considered under the PPEA, it must meet the definition of a “qualifying project” as defined in Code of Virginia, Section 56-575.1.

“Qualifying project means

- (i) any education facility, including, but not limited to a school building, any functionally related and subordinate facility and land to a school building (including any stadium or other facility primarily used for school events), and any depreciable property provided for use in a school facility that is operated as part of the public school system or as an institution or higher education;*
- (ii) any building or facility for principal use by any public entity;*
- (iii) any improvements, together with equipment, necessary to enhance public safety and security of buildings to be principally used by a public entity;*
- (iv) utility and telecommunications and other communications infrastructure; or*
- (v) a recreational facility.”*

Projects Appropriate for PPEA

This broad definition allows for the use of PPEA for virtually any type of public facility or infrastructure construction project, such as construction of new facilities, additions/expansion of existing facilities, renovation, repair, and replacement projects. Five agencies have reported centrally the receipt of PPEA proposals for construction, expansion and/or renovation projects (Exhibit 1) valued at approximately \$463 million.

Exhibit 1

Agency	Project Type	Estimated Value
Department of Corrections	New Construction & Expansion	\$167.0 million
Department of General Services	New Construction & Renovation	104.5 million
Science Museum of Virginia	New Construction	\$92.0 million
Longwood University	New Construction & Renovation	\$55.0 million
Department of Mental Health, Mental Retardation, & Substance Abuse Services	New Construction	\$44.5 million
Total		\$463.0 million

The PPEA may also be used to provide various services in lieu of the public sector providing these services. Examples are operation of central heating/cooling plants, water plants, wastewater plants, preventative maintenance operations, and even operation of entire facilities. The National Council for Public-Private Partnerships (NCPPP) points out that the provision of services by the private sector on behalf of the public sector is based on the premise of utilizing each sectors' best skills and capabilities.

At the time of this report, no agency has received a PPEA proposal to provide services. Because there has been no opportunity to review the costs and benefits of a proposal for services, this report focuses only on construction projects.

Several large firms actively involved in public-private ventures in the State of Virginia were asked to define the minimum capital project value that would be of interest to pursue under PPEA. A range of \$10 million to \$30 million was reported. In addition, smaller projects in the range of \$2 million to \$5 million were also of interest, particularly where a number of them could be contracted for at one time with delivery scheduled over a number of years. Additionally, smaller and/or more specialized contractors may be interested in projects of less value when they occur within their specialty and/or region.

Agency Capital Needs

Capital needs of the Departments of Corrections, Juvenile Justice, Military Affairs, and State Police as reported in each agency's proposed 2004-2010 Six Year Capital Plan total approximately \$509.4 million over the next three biennia (Exhibit 2). Maintenance Reserve requests are not included.

Exhibit 2

Agency	Capital Need
Department of Corrections	\$357.1 million
Department of Military Affairs	\$ 81.5 million
Department of Juvenile Justice	\$ 53.8 million
Department of State Police	\$ 17.0 million
Total	\$509.4 million

The **Department of Corrections'** (DOC) list of capital needs includes approximately \$173.6 million for construction of four new facilities: St. Brides Replacement Facility Phase 2, Deerfield Expansion, and two new facilities. A PPEA proposal for these four new construction projects is currently under consideration. In addition to new construction, DOC has needs for roofs, electrical improvements, water and wastewater facilities, HVAC upgrades, construction of small buildings, and other repair and renovation projects statewide over the next six years.

The **Department of Military Affairs'** (DMA) Six-Year Capital Outlay Plan includes the need for seven new Armories around the state. Several of the Armory facilities would be combined with either an Organizational Maintenance Shop or a headquarters facility. The estimated cost of the new Armories ranges from \$5.5 million to \$24 million, with a total cost for all seven facilities of \$78.7 million. Approximately 75% of the cost of Armory construction is provided through federal grants. The federal grant portion of the cost is included in these figures, as these amounts must be appropriated.

The **Department of Juvenile Justice's** (DJJ) capital request contains a need for approximately \$29.5 million in the construction of new buildings at various existing juvenile centers over the next six years. Other needs include HVAC upgrades, water and wastewater improvements, fire safety improvements, and other repair and renovation projects statewide.

The **Department of State Police** (DSP) is in need of nine new Area Offices with a total estimated cost of \$4.9 million, for an average of \$544,000 per new office. They also have eight Area Offices that need expansion and/or renovation over the next six years. The cost estimate from their Six-Year Capital Outlay Plan for the eight Area Office expansions is \$5.6 million. Other needs of the DSP include a new Firearms Training Facility, expansion of two Firearms Training Facilities, expansion of two Division Headquarters, and renovation of the Administrative Headquarters.

Criticality of Projects

A key issue for all of these public safety capital needs is that of criticality. Not all needs expressed in these agencies' Capital Budget Requests will be selected by the executive and/or legislative branches for funding, and if selected, the project(s) may be funded in a different biennium than that requested. In order for any capital project to proceed under a PPEA process, or traditional processes, it is prioritized within the context of all other capital needs statewide. Those projects deemed most necessary get funded first and others may be re-prioritized. This is particularly important to consider during lean fiscal times. As such, only the most critical of these projects would be considered appropriate at this time for consideration under a PPEA proposal.

Financial Feasibility

Another primary consideration of using the PPEA as a method of project delivery is that of financing. Since the implementation of the PPEA, the Department of the Treasury has reviewed financing structures in connection with eleven separate proposals for four of the five projects noted earlier. The level of detail provided to Treasury has varied. Treasury reports "although the financing proposals differed considerably in their mechanisms, terms and structure, none of the financing structures would have provided a savings, in terms of the financing costs, compared with traditional Commonwealth tax-exempt borrowing through the Virginia Public Building Authority or Virginia College Building Authority."

The Department of Treasury states that if a facility can be used to generate additional third-party revenue, through rent or user fees, then a PPEA proposal may provide the Commonwealth with the use of the facility at a lower financing cost than traditional borrowing. Such a proposal has not been made to a state agency under the PPEA at this time.

Facilities needed by DOC, DJJ, DMA, and DSP have traditionally been constructed as single use facilities. The goal of the PPEA, however, is to challenge both the public (state and local) and private sectors to step out of the traditional way of thinking and develop creative solutions to public facility and infrastructure needs. An example of a very innovative shared use arrangement is reported in the September 2003 ENR Design-Build Supplement. The project is being undertaken in Stafford County, Virginia, where the locality is using a PPEA proposal to provide two new elementary schools, a new high school, day-care center, regional branch library, YMCA facility, and a senior citizen community. Sale or lease of parts of the project will help fund the public portion.

While it may be difficult to imagine shared use arrangements by third parties for public safety facilities, opportunities may exist. One public safety example may be new, renovated, and/or expanded armories. DMA reports they can, and do, share use of some armories, and that it is not necessary that DMA control the facility. Recreational uses may be very compatible with DMA's use of the facilities. DMA reports shared use with local law enforcement and State Police would also be feasible.

Another potential that may make a PPEA proposal financially feasible would involve satisfying capital needs of more than one agency. For example, a proposal could be made to handle all construction projects in a region, or all projects of a certain type statewide. A proposal of this type could involve more than just the public safety agencies. In cases where the private offeror requires the use of their financing vehicle, there could still be economies of scale of a magnitude not normally realized by state agencies that would be significant enough to reduce the overall, all-in project costs. Such a proposal has not been made to a state agency at this time, so the potential for cost savings under this scenario cannot be evaluated. In all cases, the Department of Treasury recommends the proposer be asked to decouple the financing from the project for separate analysis.

Schedule Benefits

The timing of when a project is needed is another important factor to be considered. This often times is directly related to the criticality of the project. The PPEA may allow faster delivery of projects under design-build¹ or other delivery methods not usually available to state agencies. When comparing the schedule for construction of a new prison under a PPEA process (design-build) to the traditional design-bid-build² process, DOC found the

¹ Design-build is defined by the Construction Industry Institute as an agreement between an owner and a single entity to perform both design and construction under a single contract.

² Design-bid-build is defined by the Construction Industry Institute as a traditional process where the owner contracts with a design company to deliver 100% design documents. The owner then solicits fixed price bids from contractors to perform the work.

proposed PPEA process may save up to 28 months on a project 50-month project constructed under the traditional process, or a 56% reduction in schedule.

DOC completed a second schedule comparison that assumed authorization would be given to DOC to utilize the streamlined design-build delivery method for construction of a prison. Even with DOC using design-build, the PPEA process anticipates delivering a facility by as much as 14 months (or 31%) earlier due primarily to an earlier start date under the PPEA process.

The Science Museum of Virginia estimated a 28-month time saving in delivery of a facility under the PPEA process. The Department of General Services and the Department of Mental Health, Mental Retardation and Substance Abuse Services have noted the accelerated schedules leading to earlier delivery of needed facilities as reasons for recommending proceeding with the PPEA proposals received by those agencies.

Other Potential Benefits

In addition to faster delivery of projects and the potential for cost savings described above, other benefits may include the following:

- Design-build delivery method is accepted in the construction industry as delivering improved quality, faster, and with fewer claims;
- Comprehensive Agreements can be open-ended to allow for future projects under the same agreement, saving the time and cost of going through multiple procurements;
- Some of the risk of uncertainty regarding the need for facilities can be shifted to the private sector by allowing for future projects in a Comprehensive Agreement where less lead time can be allowed for responding to an unanticipated critical need;
- Private entities can assist agencies in acquiring federal grants and funding available on some public safety and other projects;
- Multi-party transactions can be managed under the PPEA that previously would not have been feasible to undertake;
- Public safety agencies can use their assets, such as land, to reduce project costs;
- Public safety agencies can utilize private sector strengths in non-core business areas; and
- PPEA can provide a hedge against inflation by locking in construction costs sooner.

Barriers to Use of PPEA

Some of the public safety agencies included in this report have very small capital outlay staffs, and some do not have experience with design-build projects. It may be difficult for those agencies to manage the PPEA process itself, and a resulting design-build construction project. The PPEA process is new, somewhat complex, and there is a fair amount of work involved in reviewing, reporting, analyzing, etc. to move a PPEA

proposal forward. In order to effectively handle a PPEA proposal, the project needs a “champion” at the agency level. A champion could potentially be shared amongst public safety agencies, but without a champion, the process can lose momentum and a beneficial proposal could be overlooked. The time required of the Secretary of Finance, the Secretary of Administration, and the Department of Treasury is also significant. These central agencies must review and comment on all PPEA proposals that are recommended to move forward to the Detailed Phase.

Conclusion

The PPEA process has the potential to offer creative solutions to public safety needs. While it may not be appropriate for all projects, or even most projects, it is important to keep the option open for consideration. Proposals will have to be considered on a case-by-case basis to determine what benefits there are to use of the PPEA for the specific need. The more innovative the solution proposed by the private sector, the more likely it will prove to be financially advantageous. In conclusion, the Secretary of Public Safety, with the assistance of the Departments of General Services and Treasury, finds that the Public-Private Education Facilities and Infrastructure Act of 2002 can provide a feasible method of providing required facilities and related capital expenses for the Departments of Corrections, Juvenile Justice, Military Affairs, and State Police. The value of financing under PPEA proposals must be evaluated on a case-by-case basis.